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New York State's Rating Under Threat, Moody's Says (Update3)

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David Patterson, the governor of New York

Nov. 20 (Bloomberg) -- New York state's credit rating is in danger of a downgrade, which may raise borrowing costs, if spending cuts aren't part of the solution to this year's \$3.2 billion deficit, Moody's Investors Service said.

If the budget gap for the fiscal year ending March 31 isn't closed or "if action is taken but is largely one-time in nature," and the state's revenue projections for January are accurate, the Aa3 rating and stable outlook would be threatened, Moody's said.

The rating on the state's general obligation bonds is Moody's fourth highest, and is four levels above the Baa1 rating for California, the lowest rated U.S. state.

New York Governor David Paterson, 55, has pushed lawmakers to adopt his plan to cut spending by \$1.8 billion this year, and has often pointed to California's rating as an example of what could happen if they relied exclusively on one-time actions, as sought by Senate Democrats.

Since Paterson proposed his plan to close the deficit a month ago, he has battled lawmakers who want to avoid unpopular cuts in spending on education and health care, the two biggest parts of the state's budget. He wants at least 40 percent of the deficit reduction to come from spending cuts, not "gimmicks or phony estimates of revenue which don't exist," he said Wednesday.

Bond Sales

New York plans to negotiate a \$1.47 billion sale next week of bonds backed by the state's personal income tax, followed by \$351.3 million of general obligation bonds Nov. 23, through competitive bidding. The general obligation bonds are rated AA- by Fitch Investors and AA by Standard & Poor's. Bonds backed by personal income tax collections are AAA by S&P, AA- by Fitch, and aren't rated by Moody's, according to the Division of Budget.

Recurring spending cuts are important because they would help close next year's budget gap, and are a solution to the imbalance between New York's revenue and spending, Robin Prunty, a senior ratings analyst at S&P said in an interview last week. The rating company doesn't advise issuers about the appropriate mix of recurring spending cuts and one-time actions, she said.

Moody's held the state's Aa3 rating unchanged with a stable outlook on the expectation that the Legislature "will enact solutions to the budget gap" and revenue from Wall Street bonuses will exceed state projections, it said in a rating report issued Thursday. The Division of Budget expects bonuses to decline 22 percent.

Higher Borrowing Costs

Paterson has repeatedly warned that a lower bond rating would result in higher borrowing costs.

Interest rates on general obligation bonds at the top of the A category are 0.27 of a percentage point higher than yields of bonds at the top of the AA category, according to Bloomberg indexes. The state's 10-year general obligation bonds, now at the bottom of the AA category, yield about 3.54 percent, according to Bloomberg data.

In budget negotiations with leaders of the Senate and Assembly Paterson has ruled out proposals to raise cash by restructuring the state's \$3.59 billion of tobacco bonds.

A proposal for the Battery Park City Authority to sell bonds and hand the proceeds to the state has been scrapped, according to Dean Fuleihan, Secretary of the Assembly Ways and Means Committee. Instead, the authority would give the state \$200 million in cash, a proposal that state and city officials are negotiating, said Matt Anderson, a spokesman for the Division of Budget.

Cash Squeeze

Comptroller Thomas DiNapoli repeated Paterson's warnings that the state faces a cash squeeze in December in a report issued today. DiNapoli, who said last month the state could face a \$4.1 billion deficit this year, has also supported Paterson's calls for spending cuts to balance the budget.

"Revenue that was hoped for has not materialized," DiNapoli said in a statement today. The monthly cash report by his office showed total revenue was \$85.3 million less than expected in the seven months ended Oct. 30 while spending was \$390 million above projections.

New York could be \$1.4 billion short of the money it needs in December, even after borrowing from its short-term investment pool, according to a description of the state's cash crunch DiNapoli issued today. The state will continue to pay interest and principal on its bonds, though other payments could be delayed, the report said. December payments include \$2.5 billion to local governments for property tax relief, and \$1.6 billion of aid to school districts.

In September the state delayed sending \$959.1 million to the pension fund until the legally required due date of March 1, causing it to forego a \$30 million discount for early payment.

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